D.T.E. 04-70 January 21, 2005

Petition of Boston Edison Company and Commonwealth Electric Company d/b/a NSTAR Electric for Approvals Relating to the Issuance of Rate Reduction Bonds Pursuant to G.L. c. 164, § 1H.

APPEARANCES:

Robert N. Werlin, Esq.
John K. Habib, Esq.
Keegan, Werlin & Pabian, LLP
265 Franklin Street
Boston, MA 02110
FOR: BOSTON EDISON COMPANY
COMMONWEALTH ELECTRIC COMPANY
Petitioner

Thomas F. Reilly, Attorney General
By: Colleen McConnell
Joseph W. Rogers
Assistant Attorneys General
Office of the Attorney General
Utilities Division
One Ashburton Place
Boston, MA 02108
Intervenor

Mary Beth Gentleman, Esq.
Andrew D. Fagenholz, Esq.
Foley Hoag LLP
155 Seaport Boulevard
Boston, MA 02210
FOR: MASSPOWER
DARTMOUTH POWER ASSOCIATES
LIMITED PARTNERSHIP
Intervenors

Maria J. Krokidas, Esq.
Krokidas & Bluestein LLP
600 Atlantic Avenue
Boston, MA 02110

FOR: MASSDEVELOPMENT
MASSACHUSETTS HEALTH AND EDUCATIONAL FACILITIES AUTHORITY
Intervenors

TABLE OF CONTENTS

I. INTRODUCTION

On August 31, 2004, Boston Edison Company ("Boston Edison") and Commonwealth Electric Company ("Commonwealth") (jointly "Companies" or "NSTAR Electric"), filed with the Department of Telecommunications and Energy ("Department") a petition for a financing order ("Financing Order") approving the issuance of rate reduction bonds ("RRBs"), pursuant to G.L. c. 164, §§ 1G and 1H, and Boston Edison's restructuring settlement and Commonwealth's restructuring plan. The Companies propose to securitize[1] through RRBs approximately $675 million of reimbursable transition costs, consisting of (i) the payments associated with the termination of their obligations under certain purchase power agreements ("PPAs") between the Companies and MASSPOWER, and between Commonwealth and Dartmouth Power Associates Limited Partnership ("Dartmouth Power") ("Dartmouth Agreement"), (ii) the recovery of transition costs deferred by Commonwealth pursuant to its restructuring plan ("Commonwealth Deferral"), (iii) transaction costs arising in connection with the issuance of the RRBs, and (iv) the provision of any required credit enhancement (Petition at 1-2). In addition, the Companies request that the Financing Order provide for (1) the establishment of a portion of the Companies' transition charges as transition property from which the RRBs to be issued will be repaid; (2) the organization and capitalization of a special purpose entity ("SPE") by each of the Companies to which the transition property of each of the Companies will be sold; (3) the servicing of the transition charges by each of

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[1] Securitization represents the process where RRBs are issued to investors in the form of investment security that has as its collateral the transition charge payable by utility ratepayers (Exh. NSTAR-EGO at 2-4).

Boston Edison and Commonwealth; and (4) the granting of exemptions to the Companies to the competitive bid and par-value debt-issuance requirements of G.L. c. 164, §§ 15 and 15A (id.). The Department docketed this matter as D.T.E. 04-70.

The Companies estimate the initial principal amount of the RRBs to be issued will be approximately $675 million, subject to adjustment based on the timing of the closing of the PPA buyouts and of the RRB transaction (Exh. NSTAR-GOL at 8). The Companies state that the RRB transaction will result in savings for the Companies' customers by reducing the net present value ("NPV") of the future transition charge payments made by customers by $118 million[2] (Exhs. NSTAR-GOL at 28; NSTAR-GOL-1; RR-DTE-2).

II. PROCEDURAL HISTORY

Pursuant to notice duly issued, the Department conducted a public hearing and procedural conference on October 7, 2004. The Attorney General of the Commonwealth of Massachusetts ("Attorney General") filed a notice of intervention as of right pursuant to G.L. c. 12, § 11E. The Hearing Officer granted the petitions to intervene of Dartmouth Power, MASSPOWER, and MassDevelopment and Massachusetts Health and Educational Facilities Authority (jointly, the "Agencies"). The Agencies filed comments on this matter ("Comments of the Agencies") dated September 30, 2004).

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[2] The Companies initially projected ratepayer savings of $130 million (Exh. NSTAR-GOL at 28). However, the Companies later updated their savings analyses based on (1) updated fuel and energy projections in Boston Edison Company/Commonwealth Electric Company, D.T.E. 04-61 (2005) and Commonwealth Electric Company, D.T.E. 04-78 (2005), and (2) updated transaction costs for Commonwealth (Tr. 2, at 134-135). Based on the updated data, the Companies now estimate customer savings to be $118 million (RR-DTE-2).

The Department conducted evidentiary hearings on December 1 and 2, 2004. The Companies sponsored the testimony of Geoffrey O. Lubbock, vice president, financial strategic planning and policy for NSTAR Electric and Gas Company, Emilie G. O'Neil, director of corporate finance and cash management for Boston Edison and Commonwealth, and John Fernando, senior vice president in Lehman Brothers' asset backed securities group. On December 10, 2004, the Companies, the Attorney General, and the Agencies filed initial briefs. On December 17, 2004, the Companies and the Agencies filed reply briefs, and the Attorney General and Dartmouth Power filed letters in response to initial briefs. The evidentiary record consists of 38 exhibits and the Companies' responses to ten record requests.

III. STANDARD OF REVIEW

The Legislature has vested broad authority in the Department to regulate the ownership and operation of electric utilities in the Commonwealth. See, e.g., G.L. c. 164, § 76. The Department's authority was most recently amended by the Acts of 1997, c. 164 (the "Restructuring Act" or "Act").[3] Western Massachusetts Electric Company, D.T.E. 97-120, at 10 (1999). The Act authorizes the Department to issue a financing order allowing a company to securitize its reimbursable transition costs (both debt and equity) through the

[3] An Act Relative to Restructuring the Electric Utility Industry in the Commonwealth, Regulating the Provisions of Electricity and Other Services, and Promoting Enhanced Consumer Protections Therein, signed by the Governor on November 25, 1997. St. 1997, c. 164.

issuance of electric RRBs.[4] A financing order may be issued by the Department to facilitate

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[4] The term "electric rate reduction bonds" is defined as "bonds, notes, certificates of participation or beneficial interest, or other evidences of indebtedness or ownership, issued pursuant to an executed indenture, financing document, or other agreement of the financing entity, secured by or payable from transition property, the proceeds of which are used to provide, recover, finance or refinance transition costs or to acquire transition property and that are secured by or payable from transition property." G.L. c. 164, § 1(H)(a).

"Financing order" is defined as "an order of the Department. . . approving a plan, which shall include, without limitation, a procedure to review and approve periodic adjustments to transition charges to include recovery of principal and interest and the costs of issuing, servicing, and retiring electric rate reduction bonds contemplated by the financing order." G.L. c. 164, § 1(H)(a).

"Reimbursable transition costs amounts" is defined as "the total amount authorized by the Department in a financing order to be collected through the transition charge, as defined pursuant to G.L. c. 164, § 1, and allocated to an electric company in accordance with a financing order." G.L. c. 164, § 1(H)(a).

"Securitization" is defined as the use of rate reduction bonds to refinance debt and equity associated with transition costs pursuant to G.L. c. 164, § 1H.

"Transition costs" is defined as "the costs determined pursuant to G.L. c. 164, § 1G which remain after accounting for maximum possible mitigation, subject to determination by the Department." G.L. c. 164, § 1(H)(a).

"Transition charge" is defined as "the charge to the customers which provides the mechanism for the recovery of an electric company's transition costs." G.L. c. 164, §1(H)(a).

"Transition property" is defined as "the property right created pursuant to this section, including, without limitation, the right, title and interest of an electric company or a financing entity to all revenues, collections, claims, payments, money, or proceeds of or arising from or constituting reimbursable transition costs amounts which are the subject of a financing order, including those non-bypassable rates and other charges that are authorized by the department in the financing order to recover transition costs and the costs of providing, recovering, financing, or refinancing the transition costs, including the costs of issuing, servicing and retiring electric rate reduction bonds."

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the provision, recovery, financing or refinancing of transition costs. G.L. c. 164, §1H(b)(1).

Prior to issuing a financing order, the Department must have approved an electric company's restructuring plan. G.L. c. 164, § 1A(a). The restructuring plan must include, among other things, a company's strategy to mitigate the transition costs it seeks to recover through a non-bypassable transition charge. Id. Before authorizing a financing order, the Department must find that a company has demonstrated that the issuance of electric RRBs to refinance reimbursable transition costs will reduce the rates that a company's customers would have paid without the issuance of electric RRBs, and that the reduction in rates to customers equals the savings obtained by the company. G.L. c. 164, § 1H(b)(2). The company must establish, and the Department must approve, an order of preference for use of bond proceeds such that transition costs having the greatest impact on customer rates will be the first to be reduced by those proceeds. G.L. c. 164, § 1G(d)(4).

In order to approve an application for a financing order, the Department must also be satisfied that a company has (1) fully mitigated the related transition costs (including, but not limited to, as applicable, divestiture of its non-nuclear generation assets, renegotiation of existing power purchase contracts, and the valuation of assets of the company); and (2) obtained written commitments that purchasers of divested assets will offer employment to any affected non-managerial employees who were employed at any time during the

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G.L. c. 164, § 1H(a).

three-month period prior to the divestiture, at levels of wages and overall compensation no lower than the employees' prior levels.[5] G.L. c. 164, § 1G(d)(4).

IV. NSTAR ELECTRIC'S SECURITIZATION PROPOSAL

A. Introduction

Securitization is a way for a company to refinance transition costs at a lower carrying charge rate. The Act authorizes an electric company to securitize its transition costs by issuing electric RRBs to investors that will be repaid through a portion of the transition charge. G.L. c. 164, § 1H.[6] If assigned a high credit rating,[7] the RRBs will be issued at an interest

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[5] In addition, the Department cannot approve a company's application for securitization if the company owns, in whole or in part as of July 1, 1997, a nuclear-powered generation facility located in the Commonwealth that exceeds 250 megawatts in size, unless the company has executed a tax agreement with the plant's host community. G.L. c. 59, § 38H(c). Neither Boston Edison nor Commonwealth own such a facility.

[6] RRBs are a type of security backed by the identifiable asset of the transition property, which is the right to receive cash flows generated from the billing and collection of a legislatively-mandated, non-bypassable reimbursable transition cost charge (Exh. NSTAR-JF at 3). As a result of the combination of a secure source from an identifiable cash flow, and remoteness from a utility's credit and bankruptcy risks, RRBs are generally perceived to have low risks, and therefore can be used to capitalize an asset (id.).

[7] The rating of a bond is determined by quantifying the risk associated with the likelihood of timely payment of interest and ultimate repayment of principal by the final legal maturity date (Exh. NSTAR-JF at 8). Credit enhancements reinforce the likelihood that payments on the special purpose entity debt securities will be made in accordance with the expected amortization schedule (id. at 12-13). Credit enhancements can include true-up adjustments, overcollateralization, capital accounts (equity contribution), and reserve accounts, additional reserve accounts, sureties, guarantees, letters of credit, liquidity reserves, repurchase obligations, cash collateral accounts, third-party supports, or other similar arrangements (id.).

rate lower than the carrying charge paid by ratepayers in the transition charge, thereby generating savings to ratepayers[8] (Exh. NSTAR-COM-GOL-1).

The proposed Financing Order provides for the securitization of approximately $675 million of principal, consisting of: (1) approximately $527 million for the PPA buyouts, including Boston Edison's MASSPOWER PPA buyout,[9] Commonwealth's MASSPOWER PPA buyout, and Commonwealth's Dartmouth Agreement ("Dartmouth Agreement Termination Payment"),[10] (2) $141 million allocated to the Commonwealth Deferral, and (3) $6.5 million allocated to transaction costs in connection with the issuance of the RRBs, along with the provision of any required credit enhancement (Exhs. NSTAR-GOL-1; NSTAR-EGO at 20; AG-1-3; RR-DTE-2). The Commonwealth Deferral consists of approximately $120 million in transition costs associated with above-market PPAs, and the remaining $21 million of mitigation incentives and fixed charge transition costs (Exh. NSTAR-GOL at 6; Tr. 1, at 99; RR-DTE-6).[11]

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[8] The Companies use a discount rate of 6.61 percent for Boston Edison's customer savings analysis (Exh.NSTAR-BEC-GOL-2 (Update 2)), 8.20 percent for Commonwealth's customer savings analysis (Exh. NSTAR-COM-GOL-2 (Update 2)), and 7.82 percent for both Companies' power savings analysis (Exh. NSTAR-RBH-6, from D.T.E. 04-61; Exh. NSTAR-RBH-6, from D.T.E. 04-78).

[9] On this same date, the Department has issued an Order approving the buyout by Boston Edison and Commonwealth of their PPAs with MASSPOWER. Boston Edison Company/Commonwealth Electric Company, D.T.E. 04-61 (2005).

[10] On this same date, the Department has issued an Order approving Commonwealth's buyout of its PPA with Dartmouth Power. Commonwealth Electric Company, D.T.E. 04-78 (2005).

[11] Throughout this Order, we identify $675 million as the principal amount to be

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The Companies also seek exemptions from the competitive bidding requirements of G.L. c. 164, § 15, and from the par-value debt-issuance requirements of G.L. c. 164, § 15A, in connection with the sale of the RRBs (Exh. NSTAR-EGO at 28-29).

After the Act took effect, the Department, the Agencies responsible for RRB funding and issuance, the Massachusetts-based electric companies, and other interested parties, such as investment bankers and statistical rating organizations ("rating organizations"), developed a structure for a RRB transaction. Western Massachusetts Electric Company Securitization, D.T.E. 00-40, at 8 (2000); Boston Edison Company Securitization, D.T.E. 98-118, at 7 (1999). The Companies' application is based on a proposed Financing Order that was prepared in consultation with the Agencies and is based on the previous Massachusetts RRB issuance by Boston Edison (Exh. NSTAR-EGO at 2, citing D.T.E. 98-118).

The Companies seek to recover reimbursable transition cost ("RTC") amounts that will be financed through the issuance of RRBs (Exh. NSTAR-EGO at 3-4). A portion of the Companies' respective transition charges, the RTC charges, will be used to repay these amounts (Exh. NSTAR-EGO at 3). The RRBs will be backed by collateral, including the right to all collections or proceeds arising from (a) recoverable transition costs, (b) the RTC charge,

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[11](…continued)

securitized; however, we recognize that the amount to be securitized is subject to adjustment based on the timing of the Companies' buyout of the underlying PPAs, the timing of the issuance of the RRBs, the amount of the Commonwealth Deferral at the time of issuance of the RRBs, the actual transaction costs, and input from rating agencies.

and (c) adjustments to the RTC charge (collectively, the "Transition Property") as set forth in the Financing Order (id. at 3-4).

Each Company will sell the Transition Property to a SPE (id. at 3). Each SPE will be a bankruptcy-remote entity owned and initially capitalized by the Companies, with Boston Edison and Commonwealth each establishing its own separate SPE (id.). To raise the funds to buy the Transition Property from the Companies, each SPE will issue and sell SPE debt securities to a special purpose trust established by the Agencies (id. at 6). This special purpose trust will issue RRBs, the proceeds of which will be remitted to the SPE and ultimately to the Companies (id.).

In order to maximize the savings obtainable from securitization, the RRBs must achieve the highest possible ratings. D.T.E. 98-118, at 9. The RRBs will receive ratings from national rating organizations (Exh. NSTAR-EGO at 2). A credit rating analysis takes into account elements that are customary in an asset securitization and combines them with a detailed analysis of the regulatory and legal foundation of the asset account and the collection mechanisms (Exh. NSTAR-JF at 4). Rating organizations will consider the following characteristics of RRBs: (1) bankruptcy-remoteness of the seller, (2) predictability and non-bypassability of the RTC charge, (3) standards governing a third-party supplier, (4) credit enhancement, (5) the assurance of irrevocability by the Commonwealth of Massachusetts, and (6) other statutory safeguards (id.).

The Act establishes the Agencies as a financing entity for RRBs. G.L. c. 164,

§ 1H(a). In this capacity, the goal of the Agencies is to protect the interests of the Companies' ratepayers by: (1) ensuring the lowest all-in cost pricing reasonably obtainable for RRBs, (2) streamlining the administrative processes, thereby minimizing the costs of issuing the RRBs, and (3) consulting with the Department on the issuance of the RRBs. G.L. c. 164, § 1H(b)(2). The Agencies will approve the terms and conditions of the RRBs, including structure, pricing, credit enhancement, relevant issuance costs, and manner of sale (Exh. NSTAR-1B at A-33-34). In addition, in order to minimize the all-in costs of the RRBs and associated administrative expenses, the Agencies will coordinate with the Companies regarding the marketing of the RRBs, the procurement of bond trustees and related services, and the selection of rating organizations and the underwriting syndicate (id.; Agencies Brief at 3).

The Act requires the Department to find that specific conditions have been met in order for a company to be eligible to issue RRBs. D.T.E. 00-40, at 10; D.T.E. 98-118, at 11. Specifically the Act requires that an electric company seeking securitization must establish that: (i) it has fully mitigated the related transition costs; (ii) savings to ratepayers will result from securitization; (iii) all such savings derived from securitization shall inure to the benefit of ratepayers; and (iv) it has established an order of preference for the use of bond proceeds such that transition costs having the greatest impact on customer rates will be the first to be reduced by those proceeds.[12] G. L. c. 164, § 1G(d)(4).

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[12] G.L. c. 164, § 1G(d)(4) also includes a requirement relating to employment commitments that does not apply to this proceeding.

Consistent with the requirements of the Act, the Department's analysis of the Companies' securitization proposal will focus on (1) the mitigation of transition costs, (2) the savings to ratepayers, and (3) the order of preference for use of the proceeds.

B. Mitigation of Transition Costs

1. Introduction

The Act requires a company to have an approved restructuring plan that establishes its overall mitigation strategy and to divest its non-nuclear assets in order to be able to securitize its reimbursable transition costs. G.L. c. 164, §§ 1A(a), 1G(d)(3). Before approving the recovery of transition costs through the transition charge, the Department must also issue an order finding that each of the Companies has taken "all reasonable steps to mitigate to the maximum extent possible the total amount of transition costs" each of the Companies seeks to recover. G.L. c. 164, §1G(d)(1).

2. Positions of the Parties

a. Attorney General

The Attorney General argues that the Department should reject the Companies' proposal to include the Dartmouth Agreement Termination Payment as part of the principal amount to be securitized because Commonwealth has not mitigated those costs (Attorney General Brief at 4). The Attorney General maintains that the Companies' updated analyses in D.T.E. 04-78 based on recent energy and fuel price forecasts[13] show that not only would the

[13] During the D.T.E. 04-78 proceeding, Commonwealth filed updated fuel and energy forecasts contained in the fall 2004 Henwood forecast, as well as updated

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Dartmouth Agreement fail to provide economic savings to customers, but that the Dartmouth Agreement, on a stand-alone basis, would cost customers (Attorney General Brief at 5, citing D.T.E. 04-78, RR-AG-1, Att. RR-AG-1(c)(CONFIDENTIAL)).

b. Dartmouth Power

Dartmouth Power opposes the Attorney General's position to exclude in the amount to be securitized the Dartmouth Power Termination Payment (Dartmouth Power Reply Brief at 1). According to Dartmouth Power, the Attorney General's position has already been argued in D.T.E. 04-78, and should not be reargued in this proceeding (id.). Furthermore, Dartmouth Power contends that the position of the Attorney General is not supported by the facts in D.T.E. 04-78, because the Dartmouth Agreement is one, integrated transaction and cannot be split into two transactions as maintained by the Attorney General, and because the Dartmouth Agreement, including securitization, results in savings to ratepayers (id. at 2). In addition, Dartmouth Power argues that the Attorney General's position contravenes the terms of the Act (id.). Finally, Dartmouth Power maintains that removing the Dartmouth Agreement Termination Payment from the amount to be securitized would increase the effective interest rate on the remaining amounts to be securitized (id.). Dartmouth Power urges the Department to include the Dartmouth Agreement Termination Payment in the amount to be securitized (id. at 3).

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[13](…continued)
customer-savings estimates. D.T.E. 04-78, at 5, 23.

c. The Companies

The Companies assert that they have fully mitigated all transition costs that they propose to securitize in accordance with G.L. c. 164, § 1G(d)(4)(i), which requires that electric companies have an approved restructuring plan that establishes its overall mitigation strategy and to divest its non-nuclear generation assets in order to take advantage of securitization (Companies Brief at 8). The Companies further noted that they have divested their non-nuclear and nuclear generation assets and that the Department has approved both Companies' mitigation strategies (Companies Brief at 8, citing D.T.E. 98-118, Finding No. 35; Cambridge Electric Light Company/Commonwealth Electric Company, D.T.E. 98-78/83 (1998); Boston Edison Company, D.P.U./D.T.E. 96-23 (1998); Cambridge Electric Light Company/Commonwealth Electric Company/Canal Electric Company, D.P.U./D.T.E. 97-111 (1998) and D.P.U./D.T.E. 97-111-A (1998)). In addition, the Companies maintain that if their petition is approved, the liquidation payments associated with the buyouts of MASSPOWER and Dartmouth Power PPAs will constitute reimbursable transition costs (Companies Brief at 9). The Companies also argue that the Department has already determined that each of the types of costs included in Commonwealth's deferred transition charges are those types for which the Act allows recovery (id., citing RR-DTE-3, RR-DTE-6).

The Companies assert that the Attorney General's argument opposing the proposal to include the Dartmouth Agreement Termination Payment as part of the principal amount to be securitized is flawed because: (1) it does not evaluate the overall net savings of the

renegotiated PPAs as measured as "reductions in the transition charges," and (2) it neglects to state that the securitization of the buy-out amounts is a condition precedent to the Dartmouth Agreement (Companies Reply Brief at 3, citing Exh. NSTAR-1B App. A at 4-5. [D.T.E. 04-78]). The Companies argue that the proposed Dartmouth Agreement meets the requirements of the Act, because, with securitization, customers will receive a projected $13 million NPV in savings (Companies Reply Brief at 4, citing G.L. c. 164, §§ 1G(d)(2)(i) and (ii)). Therefore, the Companies maintain that the Department should include the Dartmouth Agreement Termination Payment in the securitization principal amount (Companies Reply Brief at 4).

3. Analysis and Findings

The Department has previously approved the restructuring plans (including mitigation strategies and transition costs) of Boston Edison and Commonwealth. Boston Edison Company, D.P.U./D.T.E. 96-23; Commonwealth Electric Company, D.T.E. 97-111; Commonwealth Electric Company, D.T.E. 97-111-A. The Department has also approved the mitigation efforts of Boston Edison. D.T.E. 98-118; Boston Edison Company, D.P.U./D.T.E. 97-113 (1998); Boston Edison Company, D.T.E. 98-119/126; Boston Edison Company, D.T.E. 99-78 (2000). Further, the Department has approved the mitigation efforts of Commonwealth. Commonwealth Electric Company, D.T.E. 99-90 (2000); Cambridge/Commonwealth Electric Company, D.T.E. 00-83 (2000); Cambridge/Commonwealth Electric Company, D.T.E. 01-79 (2001): Cambridge/Commonwealth Electric Company, D.T.E. 02-80B-1 (2004). In addition, the

Department has approved divestiture of the Companies' non-nuclear and nuclear assets, which is a requirement for securitization. D.T.E. 98-118; Boston Edison Company, D.P.U./D.T.E. 97-113 (1998); Boston Edison Company, D.T.E. 98-119/126; Boston Edison Company, D.T.E. 99-78 (2000); Cambridge/Commonwealth, D.T.E. 98-78/83 (1998).

Regarding whether Commonwealth has demonstrated that the Dartmouth Agreement Termination Payment has been mitigated, and therefore should be included in the Companies' proposed securitization, this issue of mitigation was addressed in D.T.E. 04-78. There the Department found, "[b]ecause the Dartmouth Agreement, once securitization has occurred, is likely to achieve savings for ratepayers and because the savings mitigate Commonwealth's transition costs, the Department finds that the transaction is in the public interest and consistent with the requirements of G.L. c. 164, § 1G(d)(2)(ii)." D.T.E. 04-78, at 25. The Companies have demonstrated that the Dartmouth Agreement Termination Payment is mitigated, and therefore the Department approves NSTAR Electric's request to include the Dartmouth Agreement Termination Payment in the principal amount to be securitized.

Accordingly, consistent with our finding in D.T.E. 04-78 and D.T.E. 04-61, the Department finds that the Companies have taken all reasonable steps to mitigate to the maximum extent possible the total amount of transition costs that will be recovered. G.L. c. 164, § 1G(d)(1).

C. Savings to Ratepayers

1. Introduction

The Companies have indicated that ratepayer savings of $118 million will result from the issuance of the RRBs (RR-DTE-2). The Companies calculate the savings from this transaction by comparing transition costs under two scenarios: (1) no securitization of transition costs with traditional carrying costs applied, and (2) securitization of $675 million of transition costs at an assumed securitization rate of 4.5 percent (Exhs. NSTAR-GOL at 16-17; NSTAR-GOL-1; RR-DTE-2).[14]

2. Positions of the Parties

a. Attorney General

The Attorney General states that the Department should order the Companies to use one discount rate for all of the customer saving analyses in the securitization transaction Issuance Advice Letters (Attorney General Reply Brief at 2, citing Companies Brief at 11). Noting that the Companies use a discount rate of 6.61 percent for Boston Edison's customer savings analysis, 8.20 percent for Commonwealth's customer savings analysis, and 7.82 percent for

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[14] At the request of the Department, the Companies broke down the total savings estimate into "power savings" stemming from the buyout of the MASSPOWER PPAs (D.T.E. 04-61) and Dartmouth PPA (D.T.E. 04-78) and "securitization savings" stemming from the issuance of the RRBs (RR-DTE-1). Power savings were calculated by comparing the cost to terminate the PPAs, excluding securitization costs, against the projected costs of remaining in the contracts (RR-DTE-1; RR-DTE-2). Securitization savings were calculated by comparing the cost to ratepayers of the 4.5 percent issuance rate associated with the RRBs, to the carrying charge rates for transition costs in Commonwealth's restructuring plan and Boston Edison's settlement agreement (Exh. NSTAR-GOL at 16-17; RR-DTE-1; RR-DTE-2).

both Companies' above-market cost analysis, the Attorney General argues that although the customers' discount rate is difficult to estimate, it should not vary across Companies and across transactions (Attorney General Reply Brief at 2, citing D.T.E. 04-61, Exh. NSTAR-RBH-6 (CONFIDENTIAL) at 1, n.1; D.T.E. 04-78, Exh. NSTAR-RBH-6 (CONFIDENTIAL), at 1, n.1). The Attorney General contends that "with the merger of these Companies," different discount rates should not be used (Attorney General Reply Brief at 2).

The Attorney General further contends that because the average customer's marginal cost of capital and discount rate is higher than that of a large utility like NSTAR Electric, the Department should order the Companies to use a uniform discount rate that is greater than that of NSTAR Electric (Attorney General Reply Brief at 2). Reasoning that the Companies used an 8.20 percent discount rate for Commonwealth's customer savings analysis, and that the use of this discount rate would provide a minimal 58 basis point premium over the Companies' marginal cost of capital, the Attorney General concludes that the Department should order the Companies to use the 8.20 percent discount rate in all of the customers savings analysis executed for the Issuance Advice Letters (Attorney General Reply Brief at 2, citing D.T.E. 04-61, Exh. NSTAR-COM-GOL-2; D.T.E. 04-78, Exh. NSTAR-COM-GOL-2).

b. The Companies

The Companies assert that, based on the assumptions and methodology set forth in testimony, the RRB transaction will result in significant net savings to the Companies' customers by reducing the future transition charge payments its customers would be required to pay if the Financing Order were not adopted (Companies Brief at 11, citing

Exh. NSTAR-GOL at 16). Furthermore, the Companies argue that based on the evidence presented in this proceeding, the RRB transaction will result in savings for customers as is contemplated by the Boston Edison settlement agreement and the Commonwealth restructuring plan, and the Act (id., citing G.L. c. 164, §§ 1G(d)(4) and 1H(b)(2)).

3. Analysis and Findings

In order to approve a financing order, the Department must find that savings to ratepayers will result from securitization and that all such savings derived from securitization will inure to the benefit of ratepayers. G.L. c. 164, §§ 1G(d)(4)(ii)-(iii).

The record permits us to find, and we so find, that a total of $118 million of savings to ratepayers will likely result from the securitization[15] (RR-DTE-2). Some of this is attributable to power savings and some is attributable to securitization savings (RR-DTE-1; RR-DTE-2). Power savings are achieved when a PPA buyout, taken in its totality, produces a more favorable outcome than remaining with the PPA (Exh. NSTAR-RBH-6 [D.T.E. 04-61]; Exh. NSTAR-RBH-6 [D.T.E. 04-78]). That condition exists here. In D.T.E. 04-61, the Department approved NSTAR Electric's buyout of the MASSPOWER PPAs, finding that the transaction was likely to achieve savings for customers. D.T.E. 04-61, at 24. As stated above, in D.T.E. 04-78, the Department approved the Dartmouth Agreement, finding that the transaction, together with securitization, was likely to achieve savings for customers. D.T.E. 04-78, at 25. Furthermore, savings from securitization result because ratepayers will

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[15] The Department notes that no party argued that the securitization would not produce savings for customers.

be paying a lower transition charge than they would have paid without securitization (Exh. NSTAR-GOL at 14). That is, customers would not pay the carrying charge of the Companies (e.g., 8.20 percent for Commonwealth and 6.61 percent for Boston Edison), but, because of securitization, customers would pay the lower carrying charge rate of 4.5 percent (Exh. NSTAR-GOL at 15-16). Because the Companies have demonstrated savings, the Department finds that savings to ratepayers result from the proposed securitization. Therefore, the Companies should proceed with securitization and ensure that all such savings will inure to the benefit of ratepayers, in accordance with G.L. c. 164, §§ 1G(d)(4)(ii)-(iii).

Although the Companies forecast savings to ratepayers of approximately $118 million, the Department notes that the actual amount of ratepayer savings is predicated on market conditions at the time of bond issuance (Exh. NSTAR-GOL at 28). On issuance, a financing order is irrevocable and may not be altered by the Department. G.L. c. 164, § 1H(b)(3). Although the issuance of the RRBs is contingent on savings to customers, pursuant to the Act, the Department must rely on the Agencies, as the financing entity, to ensure that the maximum level of ratepayer savings is obtained. G.L. c. 164, §§ 1H(a), 1H(b)(2); D.T.E. 98-118, at 16; D.T.E. 00-40, at 15.

With respect to the Attorney General's argument that the Companies should be compelled to use a single, universal discount rate in the instant case, the Department rejects the

Attorney General's proposal for the following reasons.[16] Although Boston Edison and Commonwealth are owned by the same holding company, they are still separate companies with different risks, so different discount rates are appropriate.[17] The Department recognized this difference in approving the specific discount rate for each company. See Boston Edison Company, D.P.U./D.T.E. 96-23; Commonwealth Electric Company, D.P.U./D.T.E. 97-111. Because the Department has found that different discount rates apply to each of the Companies, a universal discount rate, as called for by the Attorney General, does not recognize the disparity in risk between the Companies, it will not be applied in this case. Therefore, it is appropriate for the Companies to use different discount rates in the calculation of customer savings.[18]

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[16] The Department notes that, although discount rates were discussed in the proceeding (see Tr. 1, at 38-39; Tr. 2, at 198-199), the Attorney General has raised the issue of a universal discount rate on Reply Brief, and, therefore, no other party had the opportunity to comment.

[17] The Attorney General argues that "with the merger of these companies, the Company should not use different discount rates for their customers" (Attorney General Reply Brief at 2). The Department notes that Boston Edison and Commonwealth have not merged, as referenced by the Attorney General.

[18] The Attorney General contends that the average customer's "marginal cost of capital" is higher than that of a large utility, but cites to no record evidence to support this point (Attorney General Reply Brief at 2), and therefore, in the absence of substantial evidence, the Department declines to accept it.

D. Order of Preference for Use of Proceeds

1. Introduction

Before the Department may approve a financing order, a company must show that it has established an order of preference for the use of the proceeds that affects its customer's rates most favorably. G.L. c. 164, § 1G(d)(4)(v). In their petition, the Companies outlined their expected use of the proceeds from the issuance of the RRBs as follows: (a) to fund the liquidation payments to MASSPOWER and Dartmouth Power, in connection with the termination of the PPAs, (b) to provide any credit enhancement required for the RRBs other than to the funding of the capital subaccount, (c) to reduce the Commonwealth Deferral,[19] and (d) to pay transaction costs (Petition at ¶ 24).

2. Positions of the Parties

a. Attorney General

The Attorney General argues that the Department must ensure that Commonwealth uses the proceeds from the bond issuance in a manner that lowers transition costs, giving preference to those providing the greatest amount of savings to customers (Attorney General Brief at 11, citing G.L. c.164, § 1H). The Attorney General argues that Commonwealth indicates that it intends to use the proceeds remaining after making any PPA termination payments to pay down only long-term debt, thus increasing Commonwealth's overall weighted cost of capital (id. at 11-12, citing Tr. 2, at 206). The Attorney General contends that the Department should

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[19] The Commonwealth Deferral of $141 million stems from its under-collection of its transition costs (Tr. 1, at 87-90).

order Commonwealth to use available funds from the bond issuance to reduce both its debt and equity and, thereby, decrease its overall weighted cost of capital (id. at 12; Attorney General Reply Brief at 2-3).

b. The Companies

The Companies state that G.L. c. 164, § 1G(d)(4)(v) requires an electric company to establish an order of preference such that transition costs having the greatest effect on customer rates will be the first to be reduced by the securitization (Companies Brief at 11). The Companies maintain that in this proceeding they propose to securitize all of the reimbursable transition costs that the Companies believe may be securitized at this time (id.). The Companies further state that they are currently securitizing only the transition costs they believe: (1) are susceptible to securitization; and (2) would generate savings resulting in lower transition charges (id. at 12, citing Exh. NSTAR-GOL at 13-14). The Companies conclude that they have established an order of preference such that the transition costs having the greatest impact on customer rates be the first to be reduced by securitization in compliance with G. L. c. 164, § 1G(d)(4)(v) (id. at 11).

The Companies contend that the Attorney General's argument that the cash proceeds from the RRBs be used to "reduce its capitalization and decrease its overall weighted cost of capital to customers" is inconsistent with the requirement in the Act that securitization be used to reduce transition costs only (Companies Reply Brief at 12). The Companies contend that because the Attorney General does not suggest how a reduction in the Companies' weighted

average cost of capital results in any reduction in transition costs, the Attorney General's request should be denied (id. at 12-13).

3. Analysis and Findings

Before the Department may approve a financing order, the Companies must show that it has established an order of preference for use of the RRB proceeds that first reduces transition costs having the greatest effect on customer rates. G.L. c. 164, § 1G(d)(4)(v).

Regarding the Attorney General's argument that the Department should order the Companies to use available funds from the bond issuance to reduce its capitalization and decrease the Companies' overall weighted cost of capital, the Act refers to an ordering of the preference for the use of proceeds to reduce transition costs. Id. The Department finds that the ordering of the proceeds that the Attorney General is requesting us to consider in the instant case are not related to transition costs, and therefore not consistent with the Act.

In D.T.E. 98-118, at 17, the Department found that Boston Edison met the requirements of the Act because all of the proposed uses of the proceeds led to equivalent customer savings levels. The Department found that the order of preference for the use of the RRB proceeds met the requirements of the Act because all of the transition costs that the proceeds were replacing had the same carrying charge, and therefore securitization of any of these transition costs had the same effect on customer rates. D.T.E. 98-118, at 17. As in that proceeding, all of Boston Edison's reimbursable transition costs have the same carrying charge rate, and all of Commonwealth's reimbursable transition costs have the same carrying charge rate (Exhs. NSTAR-BEC-GOL-2 (Update 2); NSTAR-COM-GOL-2 (Update 2)), so that the

reduction of any of those costs has the same rate effect. Accordingly, the Attorney General's recommendation regarding the order of the use of proceeds is inconsistent with the law and the record in this case, and the Department rejects the Attorney General's recommended order of proceeds. Therefore, the Department finds that the Companies' proposal satisfies the requirements of the Act relative to the order of preference for use of bond proceeds, and thus complies with G.L. c. 164, § 1G(d)(4)(v).

V. AMOUNTS TO BE SECURITIZED

A. Introduction

The Companies propose to securitize the following costs: (1) approximately $527 million for the PPA buyouts, including Boston Edison's MASSPOWER PPA buyout, Commonwealth's MASSPOWER PPA buyout, and Commonwealth's Dartmouth Agreement ("Dartmouth Agreement Termination Payment"), (2) $141 million allocated to the Commonwealth Deferral, and (3) $6.5 million allocated to transaction costs in connection with the issuance of the RRBs, along with the provision of any required credit enhancement (Exhs. NSTAR-GOL-1; NSTAR-EGO at 20; AG-1-3; RR-DTE-2). Approximately $120 million of the Commonwealth Deferral was attributable to above-market PPAs, with the remaining $21 million consisting of mitigation incentives and fixed charge transition costs (Tr. 1, at 87, 99; RR-DTE-6).

In this section of the Order we address each of the amounts to be included in the securitization principal. In addition, we will also consider the rate at which customers receive credit for mitigation charges that are included in the principal balance of the securitization.

B. Positions of the Parties

1. Attorney General

a. Dartmouth Agreement Termination Payment

The Attorney General argues that the Dartmouth Agreement Termination Payment should be excluded from the principal amount to be securitized, as the buyout amount, if considered separately from the securitization, would not provide customer mitigation (Attorney General Brief at 5, citing Exh. D.T.E. 04-78, RR-AG-1, Att.(c)(CONFIDENTIAL)). The Attorney General maintains that to approve a company's application for a financing order, the Department must be satisfied that the company has complied with the applicable transition cost mitigation requirement pursuant to G.L. c. 164, § 1G(d) (id., citing G.L. c. 164, § 1H(b)(2); D.T.E. 98-118, at 5-6).

b. Commonwealth Deferral

The Attorney General additionally argues that the Department should reject the Companies' request to include Commonwealth's unrecovered deferred transition charge in the amount to be securitized because: (1) the Department has not approved the proposed balance and (2) the proposed recovery will harm customers (Attorney General Brief at 7). The Attorney General maintains that Commonwealth should be allowed to securitize only $81 million of the proposed $141 million,[20] as the Department has approved only the former

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[20] The Attorney General uses $134 million as the amount of the Commonwealth Deferral (Attorney General Brief at 8). The source for the $134 million balance used by the Attorney General is unclear. Commonwealth reports a transition charge deferral balance of $138.7 million at December 31, 2004, and adjusts that amount to

(continued…)

figure as a result of transition charge reconciliation cases (Attorney General Brief at 8, citing Tr. 2, at 167; see Cambridge Electric Light Company/Commonwealth Electric Company, D.T.E. 02-80B-1 (2004)). As the remaining balance of approximately $60 million in transition costs has not been approved, the Attorney General contends that the Department should not allow the Companies to include this amount in the securitization (id. at 8). The Attorney General further contends that because the inflation cap on the Companies' transition charges required by the Act will be lifted on March 1, 2005, Commonwealth will have an alternative to securitization through which to recover the outstanding balance in transition costs (id.). The Attorney General argues that the Companies can raise the transition cost recovery rate, thereby reversing the savings associated with the securitization of the deferred transition charge balance and presenting the potential to over-collect (id. at 8-9, citing Western Massachusetts Electric Company, D.T.E. 03-34 (2004); Cambridge Electric Light Company, D.T.E. 01-79 (2001)).

Assuming the interest rate on the bond issuance is the proposed 4.5 percent, the Attorney General maintains that the Department should allow the Companies to include the unrecovered fixed component transition charge in the principal balance to be securitized, because the Companies have fully mitigated these fixed component costs and their securitization creates customers savings (id. at 7, citing Exh. NSTAR-GOL at 6).

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[20](…continued)
$141 million to account for such items as interest up to the closing date and certain tax consequences (Exh. NSTAR-COM-GOL-1, at 1).

c. Transaction Costs

The Attorney General notes that the Companies' proposal includes some estimates of future transaction costs that have not been incurred nor invoiced, and therefore cannot be shown to be fully mitigated (Attorney General Brief at 11, citing Tr. 1, at 48-49). The Attorney General contends that the Department should include in the securitization balance only those transaction costs associated with securitization that have been invoiced and found reasonable by the Department (id.).

d. Mitigation Incentive

The Attorney General contends that the Department should reject the Companies' proposal to securitize the Commonwealth mitigation incentive payments that it expects to receive as a result of the PPA buyouts (id. at 6-7). According to the Attorney General, in determining the amount to be securitized, the Companies calculate the NPV of that amount using a 4.5 percent discount rate rather than the 8.20 percent customer discount rate that it used to calculate customer savings (id., citing Exh. NSTAR-GOL-1, at 2). The Attorney General contends that using a lower discount rate increases the NPV, and therefore the Companies' refinancing proposal would increase rather than decrease rates (id.).

2. The Companies

The Companies contend that G.L. c. 164, § 1H(b)(1) provides that the Department may issue a financing order to facilitate the provision, recovery, financing, or refinancing of transition costs, which are defined as the embedded costs which are determined to be recoverable through a transition charge (Companies Brief at 9). According to the Companies,

the Department approved Boston Edison's transition costs and transition charges in its restructuring settlement; the Department approved Commonwealth's transition costs and transition charges in its restructuring plan (id.). Furthermore, the Companies maintain that the Act allows the Department to authorize a company to securitize reimbursable transition costs (id., citing G.L. c. 164, § 1H). The Companies argue that they propose to securitize only those reimbursable transition costs that have been, or will be, approved by the Department (id.). The amount the Companies propose to securitize, $675 million, is subject to adjustment based on the timing of the Companies' buyout of the PPAs, the timing of the issuance of the RRBs, the amount of the Commonwealth Deferral at the time of the issuance of the RRBs, the actual transaction costs, input from rating agencies, and changes in the proposed RRB transaction not now anticipated by the Companies (id. at 9-10, citing Exh. NSTAR-GOL at 8).

a. Dartmouth Agreement Termination Payment

The Companies argue that the proposed Dartmouth Agreement meets the requirements of the Act in that, with securitization, customers will receive a projected $13 million NPV in savings (Companies Reply Brief at 4, citing G.L. c. 164, § 1G(d)(2)(i) and (ii)). Therefore, according to the Companies, the Department should include the Dartmouth Agreement Termination Payment in the amount to be securitized (Companies Reply Brief 4).

b. Commonwealth Deferral

Regarding the Commonwealth Deferral, the Companies contend that the Department has determined that each of the types of costs claimed by Commonwealth as transition costs in its restructuring plan are those types of costs for which the Act allows recovery (Companies

Brief at 9, citing G.L. c. 164, § 1G). In addition, the Companies argue that the Department has approved the amount of the transition costs being recovered by Commonwealth through the end of 2002 (id. at 10, citing RR-DTE-3; RR-DTE-6). According to the Companies, the reconciliation of the amount of transition costs being recovered or expected to be recovered by Commonwealth during 2003 and 2004 has not yet been approved by the Department; however, these costs are subject to a process where the Department reviews and can approve these costs (id., citing G.L. c. 164, § 1G(a)(2)). Finally, the Companies contend that to the extent that reimbursable transition cost amounts previously included in a financing order exceed the correct amount, Commonwealth must provide customers with a uniform rate credit through their annual transition charge update (id., citing G.L. c. 164, § 1G(a)(2)). The Companies state that in Boston Edison's initial securitization proceeding, the Department explicitly approved the securitization of estimated transition costs, subject to reconciliation (Companies Reply Brief at 8, citing D.T.E. 98-118, at 25-27). Regarding the Attorney General's contention that Commonwealth can recover the deferral by increasing its transition charge after the rate cap is lifted, the Companies argue that securitization of the deferral allows Commonwealth's customers to avoid a large rate increase (id.). Finally, the Companies assert that they have demonstrated that there is a substantial reduction in the transition charge, and associated customer savings, that will be achieved through securitization of the entire deferral balance, and therefore, the Department should approve securitization of the entire Commonwealth Deferral balance (id. at 9).

c. Transaction Costs

Regarding transaction costs, the Companies maintain that the Act expressly provides that Transition Property includes the right to recover transition costs and certain transaction costs (Companies Brief at 10, citing G.L. c. 164, § 1H(a)). In addition, the Companies argue that most of the transaction costs associated with issuing the RRBs have been established, negotiated, or approved by the Agencies (id., citing Comments of the Agencies at 4). In response to the Attorney General's contention that only invoiced transaction costs should be included in the securitization (and not estimated costs), the Companies point out that the Act contemplates that not all transition costs (including transaction costs) will be invoiced prior to Department approval (Companies Reply Brief at 11).

d. Mitigation Incentive

The Companies state that the Attorney General's argument regarding the securitization of Commonwealth's mitigation incentive payments is without supporting record evidence (Companies Reply Brief at 6). The Companies contend that customers benefit from securitizing the combination of fixed and incentive components of the Commonwealth transition charge (id.).

3. The Agencies

Regarding transaction costs, the Agencies maintain that it is their responsibility to protect the interests of the ratepayers by assuring that listed transaction costs are reasonable,

and that they have reviewed transaction costs and ongoing administrative costs,[21] and have found them to be reasonable both in terms of the Companies' proposed transaction and by reference to the previous Boston Edison and Western Massachusetts Electric Company RRB issuances (Agencies Brief at 8; Agencies Reply Brief at 3). The Agencies further note that the Department is charged with reviewing the reasonableness of the remaining transaction costs, which will be included in the initial Issuance Advice Letter (Agencies Reply Brief at 4). Additionally, the Agencies assert that the Department will monitor the proposed recovery of the costs not reviewed by the Agencies, including ongoing transaction costs included in the RTC Charges, as well as any additional adjustment in the transaction costs as part of the annual RTC Charge routine true-up mechanism (Agencies Reply Brief at 4). There the Department may require the Companies to make an adjustment to its RTC charge so that any over- or under-collection can be addressed (id.).

C. Analysis and Findings

Because the bonds issued pursuant to this Order will be without recourse to the credit of the Companies, and because the bonds will constitute irrevocable obligations levied on bills paid by the ratepayers of Boston Edison and Commonwealth until their retirement, the Department must scrutinize all amounts proposed to be included in the securitization total to ensure that only those costs that have been shown to be recoverable and mitigated are

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[21] Fees which have been established, negotiated or approved by the Agencies include underwriting spread, rating agency fees, printing and marketing expenses, trustee fees and trustee counsel fees, underwriters' legal fees, bond counsel fees, special counsel fees, Agencies' fees, and miscellaneous costs and expenses (Agencies Brief at 8).

securitized (Exh. NSTAR-1B at A52, Finding 56). See D.T.E. 00-40, at 18; D.T.E. 98-118, at 24. Therefore, in this section, the Department will determine if the amounts that the Companies request to be included in the securitization are (1) recoverable, and (2) mitigated.

1. PPA Buyout Amounts

The Department has made the finding that the Companies have demonstrated that they have taken all reasonable steps to mitigate transition costs to the maximum extent possible. Section IV.B. The Department has also found that both the MASSPOWER buyout payment and the Dartmouth Agreement Termination Payment are recoverable and mitigated. D.T.E. 04-61, at 24; D.T.E. 04-78, at 25. Therefore, the Department finds that the Companies may include the MASSPOWER Termination Payment and the Dartmouth Agreement Termination Payment in the amount to be securitized.

2. Commonwealth Deferral

Commonwealth has accumulated its transition charge deferral because of the rate cap requirement of the Act. G.L. c. 164, § 1G(e). The Department has approved Commonwealth's transition charge deferral balance of $81 million as of December 31, 2002 (Exh. NSTAR-COM-GOL-3, at 1). Commonwealth Electric Company, D.T.E. 99-90 (2000); Cambridge Electric Light Company/Commonwealth Electric Company, D.T.E. 00-83 (2000); Cambridge Electric Light Company/Commonwealth Electric Company, D.T.E. 01-79 (2001); and Cambridge Electric Light Company/Commonwealth Electric Company, D.T.E. 02-80B-1 (2004). In these proceedings, the Department has found that the reconciliation of transition costs and revenues is consistent with Commonwealth's restructuring plan and Department

precedent, and therefore is in the public interest. Also, in Commonwealth's restructuring plan, the Department has approved the categories of transition costs that are included in the full amount of $141 million included in the Commonwealth Deferral. Cambridge Electric Light Company/Commonwealth Electric Company/Canal Electric Company, D.P.U./D.T.E. 97-111 (1998).

Regarding the Attorney General's argument that only $81 million of deferrals should be included in the amount to be securitized, the Department does not find the arguments of the Attorney General persuasive. First, the Department has previously approved securitization amounts that are based on estimates. D.T.E. 98-118, at 20, 25-27 (Department approved estimated transaction costs); D.T.E. 00-40, at 19 (Department approved estimated refinancing costs). Second, there is a reconciliation process in place to address any over- or under-collection of transition costs. Although the Department has not approved the transition charge balances for 2003 and 2004, these charges will be trued up in the Companies' transition charge reconciliation process. This regulatory mechanism will afford ratepayers sufficient protection that the amounts securitized will ultimately be examined and approved by the Department, with proper adjustments made to the Companies' transition charge balances. Therefore, the Department finds that the Commonwealth Deferral is both mitigated and recoverable, and therefore the Companies may include the requested deferral balance of approximately $141 million in the amount to be securitized.[22]

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[22] The Department addresses the mitigation incentive further, below.

3. Transaction Costs

The Agencies have reviewed the Companies' estimated transaction costs, including the costs of issuing, servicing, and retiring the RRBs, and the proposed administration and servicing fees, and have found the costs to be reasonable for the Companies' proposed transaction and in comparison with the earlier Boston Edison RRB transaction (Agencies Brief at 8). The Agencies commit to review the final transaction costs at the time of issuance and to monitor the proposed recovery of transaction costs, including ongoing transaction costs included in the RTC charge (Agencies Brief at 8).

Because the Act permits recovery of refinancing costs as Transition Property, the Department will allow the Companies to securitize the refinancing costs associated with the securitization (e.g., the unamortized loss on required debt, refinancing expenses, call or tender premiums and transaction costs). See G.L. c. 164, § 1H(a). However, the Department will review the reasonableness of these costs in the Companies' next transition charge reconciliation proceedings and may, at any time, disallow the recovery of costs that are found to be unreasonable. See D.T.E. 00-40, at 19. The Department will ensure that any disallowance of the refinancing costs will not affect the RTC charge. Furthermore, if the Companies' actual refinancing costs are lower than the securitized amount, the Department directs the Companies to return to ratepayers through the transition charge any amounts in excess of its actual costs, with carrying costs.

In prior securitizations, the Department has approved the recovery of transaction costs based on estimates, subject to true-up in an annual reconciliation process. D.T.E. 98-118,

at 22-27; D.T.E. 00-40, at 19. Consistent with this precedent, which approved transaction cost estimates, we again find that the Agencies possess the ultimate responsibility for establishing the reasonableness of fees as part of its larger responsibility of protecting ratepayers' interests. In addition, the reconciliation process affords ratepayers with sufficient protection against over-collections. Therefore, the Department rejects the Attorney General's requirement that all transaction costs be invoiced prior to inclusion within the securitization.

4. Securitization of the Mitigation Incentive

Although the Agencies are responsible for considerable oversight of the financial details of the securitization, the Department also has oversight of the transaction, particularly the reconciliation of the Companies' transition charges. D.T.E. 00-40, at 19. The Attorney General has raised the issue that the Companies have increased the amount to be securitized for Commonwealth's mitigation incentive by using a discount rate of 4.5 percent (the projected interest rate for the RRBs) rather than 8.20 percent (the rate used by Commonwealth to calculate customer savings) (Attorney General Brief at 6). Consequently, the Attorney General recommends the mitigation incentive be eliminated entirely from the principal amount to be securitized by the Companies (id.). The Department finds that eliminating the mitigation incentive from the amount to be securitized is not necessary. As stated above regarding the full Commonwealth Deferral, the continuing transition charge reconciliation process addresses any over- or under-collection of transition costs. This process affords sufficient protection to ratepayers that the amounts securitized will be examined and approved by the Department, with proper adjustments made to the Companies' transition charge balances. Therefore, we

find that the Companies may include the mitigation incentive in the principal amount to be securitized.

5. Conclusion

Based on the foregoing analysis and findings, the Department will allow the Companies to securitize approximately $675 million as follows: (1) approximately $527 million for the PPA buyouts, including Boston Edison's MASSPOWER PPA buyout, Commonwealth's MASSPOWER PPA buyout, and Commonwealth's Dartmouth Agreement ("Dartmouth Agreement Termination Payment"), (2) $141 million allocated to the Commonwealth Deferral, and (3) $6.5 million allocated to transaction costs in connection with the issuance of the RRBs, along with the provision of any required credit enhancement (Exhs. NSTAR-GOL-1; NSTAR-EGO at 20; AG-1-3; RR-DTE-2). Consistent with the Department's ruling in D.T.E. 00-40 and D.T.E. 98-118, the Companies are directed to refund any excess amounts securitized to ratepayers through a credit to the respective transition charges in an amount equal to the excess amount securitized, including carrying costs.

VI. PROPOSED FINANCING ORDER

A. Introduction

As discussed above, the Companies, in consultation with the Agencies, submitted a proposed financing order with their petition (Exh. NSTAR-1B). The proposed financing order includes reporting forms and a letter of advice ("Issuance Advice Letter") that would be filed with the Department by the Agencies at the bond issuance (id.). The issues to be addressed in

this section are: (1) the Issuance Advice Letter, (2) provision of additional data regarding the bond issuance, and (3) term of the bonds.

B. Positions of the Parties

1. Attorney General

The Attorney General seeks to have the Department require the Companies to immediately correct any errors in the calculations in the Issuance Advice Letter and/or the accompanying attachments (Attorney General Brief at 9). Further, he requests the Companies to make corrections as soon as they become known and immediately make changes to the transition charges [23] (id. at 10). The Attorney General contends that mistakes made in the Issuance Advice Letter can lead to over-recoveries that can remain with the SPEs until their dissolution, some eight to ten years after the issuance of the bonds (id. at 9-10). The Attorney General contends that the Companies' offer of correction of errors in the True-up Advice Letters is not sufficient, and errors must be corrected in the Issuance Advice Letter (Attorney General Reply Brief at 1-2).

The Attorney General contends that the Department should require the provision of Treasury debt interest rates and the premiums over those rates for each maturity date that will be used to determine the coupon rates for the bonds (Attorney General Brief at 10). According to the Attorney General, the Department will be better able to determine the reasonableness of

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[23] In fact, the Attorney General notes that other states have included in their finance orders a provision for a period of review of the Issuance Advice Letter for the regulatory authority (Attorney General Reply Brief at 2, n.2).

the interest rates on the bonds if the Companies provide additional information in the Issuance Advice Letter (id.).

Regarding the term of the bonds, the Attorney General argues that the Department should order the Companies to match the maturity of the proposed bond issue with the term of the longest lived transition cost that it is securitizing (id. at 5). According to the Attorney General, the Companies' proposal to finance the Dartmouth Agreement Termination Payment, which has twelve years remaining, with eight-year bonds, creates inter-generational cross-subsidization (id. at 6). The Attorney General notes that, "[s]imply increasing the maturity of the bonds to twelve years would mitigate the cross-subsidization, while at the same time increasing customers' net present value savings" (id.).

2. The Agencies

The Agencies recommend overall approval by the Department of the proposed Financing Order, as it relates to the issuance of RRBs (Agencies Brief at 2). The Agencies state that they will establish the "financing entity" for the RRBs, and in this capacity, the Agencies' goal is to protect the interests of the Companies' ratepayers through (1) ensuring that the all-in costs of issuing the RRBs are minimized given current market conditions, (2) streamlining the administrative process, and, thereby minimizing the costs of issuing the RRBs, in particular by combining the RRB issuances of both companies, and (3) providing expertise to the Department to insure the most cost efficient structure for the issuance of the

RRBs[24] (id., citing G.L. c.164, § 1H(b)(2)). The Agencies further note that it is their role as financing entity, not the Department, to oversee the issuance of the RRBs, and the Agencies will approve the final terms and conditions of the RRBs (id. at 3; Agencies Reply Brief at 2). The Agencies also coordinate marketing of the bonds and the procurement of bond trustees and related services, approve the Companies' selection of rating agencies, and coordinate the underwriting syndicate to minimize the all-in cost of the RRBs and associated administrative expense (Agencies Brief at 3).

The Agencies also state that the proposed structure of the Financing Order is designed such that RTC Charge collections, together with interest earnings, will be sufficient to discharge the total payment requirements of each SPE over the expected term of the transaction (id.). In addition, the Agencies maintain that the proposed Financing Order meets the legal requirements to issue RRBs, and incorporates all known provisions necessary to achieve the highest possible credit rating and thus the lowest possible interest cost for the RRBs (id. at 4). The Agencies note that the true-up mechanism proposed by the Companies for increases in the RTC Charges may require deferral of other charges (id. at 7). The Agencies also note that the Department will review the Companies' Financing Order periodically to assure the accuracy of the reimbursable transition costs amounts, and will require the Companies to issue a uniform

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[24] However, the Agencies note that they make no recommendation regarding the following matters which they contend are within the Department's authority: (I) determination and audit of reimbursable transition cost amounts; (ii) the use of RRB proceeds by the Companies; and (iii) matters related to the termination of obligations under PPAs (Agency Brief at 2, n.1).

rate credit based on usage if the total in the financing order exceeds the actual amount of reimbursable transition costs (id. at 8-9, citing G.L. c. 164, § 1G(a)(2)).

The Agencies disagree with the Attorney General's assertion that the Department should order the Companies to provide Treasury debt interest rates and premiums over those rates used to determine the coupon rates with the Issuance Advice Letter (Agencies Reply Brief at 2). The Agencies state that it is their role to oversee the issuance of the RRBs, and that they are currently overseeing the issuance of the RRBs (id.). The Agencies state that they will approve the final terms and conditions of the RRBs, in consultation with the investment banker who has served in this capacity on behalf of the Agencies in connection with prior RRB issuances and continues to serve in this RRB issuance (id.). Therefore, the Agencies conclude, that the Department should not require the provision of Treasury debt interest rates and premiums over those rates used to determine the coupon rates with the Issuance Advice Letter (Agencies Reply Brief at 2).

3. The Companies

The Companies assert that the proposed Financing Order complies with the Act, including: providing for an 18-month look-back audit; providing for a uniform rate credit; billing, and collection and remittance procedures; a mechanism to address unanticipated excess RTC charges; and terms of the draft service agreement (Companies Brief at 12-13). The Companies maintain that the proposed Financing Order contemplates that the Agencies will oversee the issuance of the RRBs (id. at 14). The Companies further note that it is the Agencies that will approve the final terms of the RRBs, including pricing, in order to ensure

that the all-in costs of issuing the RRBs are minimized given current market conditions (Companies Reply Brief at 10, citing Agencies Brief at 2). The Companies also state that the Agencies have reviewed the Companies' filing, and have given the opinion that: the petition meets the legal requirements to issue RRBs; the proposed Financing Order contains the provisions necessary for the RRBs to achieve the highest possible ratings from major rating agencies, and therefore, bear the lowest interest cost in the current rate environment; the proposed Financing Order contains third-party billing requirements of rating agencies; the proposed Financing Order contains provisions to ensure that funds will be credited to customers; and annual company servicing fees are reasonable (Companies Brief at 14-15, citing Comment of the Agencies at 2-4).

Regarding the Issuance Advice Letter, the Companies contend that it is not necessary to include in the Financing Order a provision for prompt correction of any errors in calculations (Companies Reply Brief at 9). The Companies argue that to the extent any errors occur, these amounts will be taken into account in annual or more frequent adjustments to the RTC charge (id. at 9, citing Exh. NSTAR-EGO-5). Any unanticipated over-collections would be deposited in a reserve account, and then, in turn, the amount would be included in an RTC adjustment that is made annually (id. at 10).

Regarding the provision of additional data concerning Treasury rates and spreads, the Companies argue that the provision of such data is unnecessary since the Agencies will oversee the issuance of the RRBs (id.). The Companies contend that the Agencies are to ensure that the all-in costs of issuing the RRBs are minimized given current market conditions, and that the

Agencies will approve the final terms of the RRBs, including pricing (id., citing Agencies Brief at 3).

Regarding the Attorney General's recommendation to lengthen the term of the bonds to coincide with the term of the Dartmouth PPA, the Companies assert that the proposed term for the RRBs appropriately takes into account the Department's stated goal of ensuring that customers realize the benefits of reduced transition costs as soon as possible (id. at 5, citing D.T.E. 97-111, at 75-76). The Companies maintain that the Attorney General's assertion of inter-generational cross-subsidization resulting from the Companies' proposed term for the RRBs is unfounded and insupportable, and that per the Act, transition charges are non-bypassable, i.e., that customers in general are responsible for the payment of transition costs (id. at 5, citing G.L. c. 164, § 1G(e)). The Companies note that their proposed securitization payment period is applicable to the Dartmouth Agreement Termination Payment, MASSPOWER buyout, and the Commonwealth Deferral, and, additionally, that it is impossible to match, at any given time, the generation of customers that would have paid a particular underlying transition cost with the customer that may pay the RTC Charge (id.). Finally, the Companies state that although there is no precise formula that can be applied, the Department qualitatively balances multiple factors when it considers the issue of inter-generational equity (id. at 6, citing Fitchburg Gas and Electric Light Company, D.T.E. 02-24/25, at 153 (2002); Boston Gas Company, D.P.U. 93-60-D at 4 (1994)).

C. Analysis and Findings

1. Issuance Advice Letter

Regarding the issue of correcting any errors in the Issuance Advice Letter, the Attorney General's request to amend the Financing Order to require the Companies to correct any miscalculations or errors in the Issuance Advice Letter presumes that the Department should avail itself of the authority to require immediate corrections in the Issuance Advice Letter. The Agencies have ultimate responsibility for ensuring that ratepayers receive the most advantageous terms available for the issuance of RRBs (see Agencies Reply Brief at 2), including the production of the Issuance Advice Letter. Furthermore, consistent with our determination not to set the bond maturities for the RRBs (see below, Section VI.C.3), the Department does not find it appropriate to impose procedural and regulatory requirements that impede the Agencies in attaining outcomes most advantageous to ratepayers. In addition, the Department finds that the periodic true-up/adjustment mechanisms that are currently in place are sufficient to correct errors that may occur in the Issuance Advice Letter, in subsequent Issuance Advice Letters or Attachments. Finally, the review of these data could delay or contribute additional administrative and regulatory burden. Therefore, the Department will not require the immediate correction of errors to be included in the Issuance Advice Letter as requested by the Attorney General.

2. Provision of Additional Data Regarding the Bond Issuance

Regarding the provision of additional data regarding the bond issuance, it is the responsibility of the Agencies to approve the final terms of the RRBs, including pricing, and to

perform this function in such a fashion that minimizes the costs of the offering (Agencies Brief at 2, 3; Agencies Reply Brief at 3). The Department recognizes the expertise of the Agencies in these matters and their competence in performing their duties in the previous securitization transactions. Therefore, we do not find it necessary to require that the Treasury rates and spread information be provided as requested by the Attorney General. Consequently, the Department rejects the Attorney General's request that the Department require that the Treasury rates and spread information be provided.

3. Length of Bonds Term

The Department rejects the recommendation of the Attorney General that the Companies should lengthen the maturity of the bonds from the proposed eight years to twelve years to match the term of the Dartmouth PPA. First, transition costs are stranded costs that are non-bypassable and recovered through a kilowatt-hour charge that is the same for all customer classes. G.L. c. 164, §§ 1G(a)(1) and (e). As such, transition costs by their nature are not recovered dollar for dollar by those customers that caused the costs. Second, in both the prior securitizations approved by the Department (D.T.E. 98-118 and D.T.E. 00-40), and in the instant securitization, the Agencies have pledged to ensure minimized costs for ratepayers and have pledged to pursue "the most efficient structure for the issuance of the RRBs" (Agencies Brief at 2). The Department finds that the imposition of requirements such as the term of the bonds could compromise or interfere with the ability of the Agencies to achieve their goals. Therefore, the Department rejects the suggestion of the Attorney General to lengthen the maturity of bonds issued as part of the securitization.

4. Conclusion

The Department has reviewed the proposed Financing Order (Exh. NSTAR-1B). The Department finds that the proposed Financing Order is consistent with the requirements of the Act and the findings in this Order. Therefore, the Department approves the proposed Financing Order, and incorporates that Financing Order as Appendix to D.T.E. 04-70.[25]

VII. EXEMPTIONS

A. Exemption From the Competitive Bidding Requirements

1. Introduction

The Companies request an exemption from the competitive bidding requirements of G.L. c. 164, § 15 pertaining to the issuance of debt securities (Petition at 2). The Companies argue that a complex, asset-backed securitization transaction such as this requires significant input from investment bankers in order to achieve the highest possible rating for the RRBs (Exh. NSTAR-EGO at 28; Companies Brief at 13). The Companies state that unless an investment bank had assurance that it would be retained to underwrite the RRB transaction, the investment bank would not be willing to commit the significant resources and time necessary for a successful RRB transaction (Exh. NSTAR-EGO at 28-29). Therefore, the Companies consider the competitive bidding requirements of G.L. c. 164, § 15 to materially inhibit their ability to obtain the necessary levels of input and guidance (Companies Brief at 13). No other party addressed this issue.

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[25] The Financing Order we approve today is the same as Exh. NSTAR-1B.

2. Standard of Review

Pursuant to G.L. c. 164, § 15, an electric or gas company offering long-term bonds or notes in excess of $1,000,000 in face amount payable at periods of more than five years after the date thereof must invite purchase proposals through newspaper advertisements. The Department may grant an exemption from this advertising requirement if the Department finds that an exemption is in the public interest. G.L. c. 164, § 15. The Department has found it in the public interest to grant an exemption from the advertising requirement where there has been a measure of competition in private placement. See, e.g., Berkshire Gas Company, D.P.U. 89-12, at 11 (1989); Eastern Edison Company, D.P.U. 88-127, at 11-12 (1988); Western Massachusetts Electric Company, D.P.U. 88-32, at 5 (1988). The Department also has found that it is in the public interest to grant a company an exemption from the advertising requirement when a measure of flexibility is necessary in order for a company to enter the bond market in a timely manner. See, e.g., D.P.U. 88-32, at 5. However, G.L. c. 164, § 15 requires advertising as the general rule, and waiver cannot be automatic, but must be justified whenever requested. Bay State Gas Company, D.T.E. 02-73, at 14.

3. Analysis and Findings

In D.T.E. 98-118, at 42-43, the Department approved Boston Edison's request for an exemption from the requirements of G.L. c. 164, § 15, citing the limited ability to obtain service from entities sufficiently familiar with utility asset-backed securities, as well as the

increased flexibility offered by a negotiated process.[26] In this case, the Companies have demonstrated that securitization financings are highly structured, complex, multi-party undertakings requiring expertise in a wide range of areas, including transaction structuring, financial analysis, system and data requirements, rating agency negotiations, investor education, and marketing and distribution (Exhs. NSTAR-JF, at 2; NSTAR-EGO-2; NSTAR-EGO at 20-21). In addition, the Companies have also demonstrated that, given the level of preparation work that would be required, entities providing such services would likely do so only if the provider had a high degree of assurance that their firm would be selected to market and issue the RRBs (Exh. NSTAR-EGO at 28-29). The Department finds that the Companies have shown that a competitive bid process could deter underwriter assistance, a critical element of a successful RRB transaction; this lack of underwriter assistance may reduce the ability of the Companies to execute a successful RRB transaction, possibly denying the benefits of securitization to ratepayers. See D.T.E. 98-118, at 42-43; D.T.E. 00-40, App. 1 at 38.

Furthermore, the competitive bidding requirement is inconsistent with the role of the Agencies in this transaction. It is the Agencies in their role as financing entity, not the Department, that oversee the issuance of the RRBs, including approval of the final terms and conditions of the RRBs (Agencies Reply Brief at 2; Exh. NSTAR-1B at A-33). The Agencies also coordinate marketing of the bonds and the procurement of bond trustees and related

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[26] To date, 20 utilities in nine states, including Massachusetts, have successfully issued RRBs; each of these transactions received triple A ratings from two or more nationally recognized rating agencies (Exh. NSTAR-JF at 4).

services, approve the Companies selection of rating agencies, and coordinate the underwriting syndicate to minimize the all-in cost of the RRBs and associated administrative expense (Agencies Brief at 3; Exh. NSTAR-1B at A-33, A-34). See also D.T.E. 04-51, D.T.E. 04-74 (role of Massachusetts Development Finance Agency). The Department finds that the Companies have demonstrated the benefits of a competitive solicitation process are enjoyed by their ratepayers through the structure of the RRB transaction, and that requiring a competitive solicitation process could ultimately jeopardize the securitization process itself. See D.T.E. 98-118, at 42-43. Therefore, based on the foregoing analysis, the Department finds that it is in the public interest to exempt the Companies from the competitive bidding requirements of G.L. c. 164, § 15.

B. Exemption From G.L. c. 164, § 15A

1. Introduction

The Companies request a exemption from the par value debt issuance requirement of G.L. c. 164, § 15A (Petition at 2). According to the Companies, such an exemption would be in the public interest because it is difficult to price the RRBs at par value at all times and still achieve the lowest interest rate available for securitization (Exh. NSTAR-EGO at 29; Companies Brief at 14). The Companies maintain that the requested exemption will allow the Companies to issue the RRBs regardless of the daily changes in the financial markets (Exh. NSTAR-EGO at 29; Companies Brief at 14). The Companies further argue that without the ability to set the effective interest rate most precisely through a small discount on the par value of the RRBs, the Companies could have to pay a slightly higher interest rate to sell the

RRBs resulting in lower savings to ratepayers (Exh. NSTAR-EGO at 29; Companies Brief at 14). No other party addressed this issue.

2. Standard of Review

Pursuant to G.L. c. 164, § 15A, a company is required to sell long-term bonds, debentures, notes, or other evidence of indebtedness at no less than the par value or face amount unless sale at less than par value is found by the Department to be in the public interest. See, e.g., Boston Edison Company, D.P.U. 91-47, at 13 (1991). The Department has found that it is in the public interest to grant an exemption from the par value requirement where market conditions make it difficult at times for a company to price a particular issue at par value and simultaneously offer an acceptable coupon rate to prospective buyers. Bay State Gas Company, D.P.U. 91-25, at 9 (1991). The Department also has found that it is in the public interest to authorize the issuance of debt securities below par value where authorization to do so offers a company enhanced flexibility in entering the market quickly to take advantage of prevailing interest rates, particularly if enhanced flexibility promises to benefit the company's ratepayers in the form of lower interest rates and a lower cost of capital. Id.; see also Boston Gas Company, D.P.U. 92-127, at 8 (1992); D.P.U. 91-47, at 12-13. If the Department authorizes a company to issue debt securities at less than par value, the Department may establish the method by which the company is required to amortize any discount.[27] G.L. c. 164, § 15A; see, e.g., D.P.U. 92-127, at 8; D.P.U. 91-47, at 15.

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[27] The discount is the difference between the par value of a bond, note, or other debt security and the actual issue price when the actual issue price is less than par value.

3. Analysis and Findings

The Department recognizes that investors rely on, and expect, discounts from par value to serve as a fine-tuning device to ensure that the coupon rate matches market expectations, thereby offering the utilities increased flexibility in placing their issuances with prospective investors. Nantucket Electric Company/Massachusetts Electric Company, D.T.E. 04-74, at 29 (2004); Berkshire Gas Company, D.T.E. 03-89, at 16-17 (2004); Bay State Gas Company, D.P.U. 91-25, at 10 (1991). The Companies have demonstrated that market conditions may make it difficult to price the RRBs at par value at all times and still realize the most favorable interest rate (Exh. NSTAR-EGO at 29). The increased flexibility afforded by discounts would enable the Companies to issue RRBs in a timely manner and take advantage of favorable market conditions. D.T.E. 98-118, at 44. For these reasons, the Department finds that it is in the public interest to exempt the Companies from the par value requirements of G.L. c. 164, § 15A.

VIII. ORDER

Accordingly, after due notice, hearing and consideration, it is

ORDERED: That the petition of Boston Edison Company and Commonwealth Electric Company, dated August 31, 2004, for approvals relating to the issuance of rate reduction bonds is hereby APPROVED; and it is

FURTHER ORDERED: That the issuance of rate reduction bonds by Boston Edison Company and Commonwealth Electric Company to securitize reimbursable transition costs amounts pursuant to this Financing Order and the Appendix to D.T.E. 04-70, which contains additional terms for the issuance of the bonds, is hereby APPROVED; and it is

FURTHER ORDERED: That the amount which Boston Edison Company and Commonwealth Electric Company may securitize comprises the costs associated with: (1) the payments associated with the termination of Boston Edison Company and Commonwealth Electric Company's obligations under certain purchase power agreements between the Companies and MASSPOWER, as approved by the Department in D.T.E. 04-61, and between Commonwealth Electric Company and Dartmouth Power Associates Limited Partnership, as approved by the Department in D.T.E. 04-78, (2) the recovery of transition costs deferred by Commonwealth Electric Company pursuant to its restructuring plan, (3) transaction costs arising in connection with the issuance of the rate reduction bonds, and (4) the provision of any required credit enhancement; and it is

FURTHER ORDERED: That Boston Edison Company and Commonwealth Electric Company's request for an exemption from the competitive bidding requirements of G.L. c. 164, § 15 is hereby APPROVED; and it is

FURTHER ORDERED: That Boston Edison Company and Commonwealth Electric Company's request for an exemption from the par value debt issuance requirements of G.L. c. 164, § 15A is hereby APPROVED; and it is

FURTHER ORDERED: That Boston Edison Company and Commonwealth Electric Company shall comply with all orders and directives contained herein.

By Order of the Department,

_____/s/_____
Paul G. Afonso, Chairman

_____/s/_____
James Connelly, Commissioner

_____/s/_____
W. Robert Keating, Commissioner

_____/s/_____
Judith F. Judson, Commissioner

An appeal as to matters of law from any final decision, order or ruling of the Commission may be taken to the Supreme Judicial Court by an aggrieved party in interest by the filing of a written petition praying that the Order of the Commission be modified or set aside in whole or in part. Such petition for appeal shall be filed with the Secretary of the Commission within twenty days after the date of service of the decision, order or ruling of the Commission, or within such further time as the Commission may allow upon request filed prior to the expiration of the twenty days after the date of service of said decision, order or ruling. Within ten days after such petition has been filed, the appealing party shall enter the appeal in the Supreme Judicial Court sitting in Suffolk County by filing a copy thereof with the Clerk of said Court. G.L. c. 25, § 5.